Contact: Maria Cilenti - Director of Legislative Affairs - mcilenti@nycbar.org - (212) 382-6655

REPORT ON LEGISLATION BY THE BANKING LAW COMMITTEE

S.5035 **Sen. Peralta**

A bill to establish the Home Mortgage Bridge Loan Assistance Act

THIS BILL IS APPROVED

This report is submitted by the New York City Bar Association in support of S.5035, a bill to establish the Home Mortgage Bridge Loan Assistance Act of 2013 ("HMBLAA," or the "Bill").[1] The purpose of the Bill is to institute a program that will provide temporary and repayable financial assistance through bridge loans to homeowners experiencing temporary difficulty in paying their mortgage loans through no fault of their own.

PURPOSE OF A BRIDGE LOAN MORTGAGE ASSISTANCE PROGRAM

New York and the nation continue to struggle in the aftermath of a sizable real estate market bubble and bust with rarely precedented wealth destructive effects. One result of this calamity is that large numbers of New Yorkers have been driven into temporary involuntary unemployment or underemployment, and in consequence have either fallen into or come close to mortgage delinquency notwithstanding that their mortgages are structurally sound and their capacities to resume payments once reemployed are unimpaired. These individuals do not necessarily need the type of assistance offered by current federal programs; rather, they would benefit from a short-term bridge loan, such as provided by the Bill.

Empirical evidence reveals that many temporarily troubled mortgage borrowers prove able to retain their homes and pay off their mortgages in full, without a loan agreement modification, when offered bridge loan assistance. For example, Pennsylvania's Homeowners' Emergency Mortgage Assistance Program ("HEMAP") has proved highly successful over the course of three decades, in cost-effectively limiting foreclosure rates and attendant economic and social ills.[2] The Bill uses HEMAP as its principal template while making a number of improvements, with the benefit of hindsight, as described below.

---

[1] The Banking Law Committee's full report on HMBLAA, "Proposal to Adopt the Home Mortgage Bridge Loan Assistance Act of 2012" (March 2012), can be accessed at: http://www2.nycbar.org/pdf/report/uploads/9_20072233-BridgeLoanAssistanceProgram.pdf.

[2] James Orr, John Sporn, Joseph Tracy and Junfeng Huang. 2011. "Help for Unemployed Borrowers: Lessons from the Pennsylvania Homeowners' Emergency Mortgage Assistance Program." Federal Reserve Bank of New York, Vol. 17, No. 2, *available at* www.newyorkfed.org/research/current_issues. (Cited herein as "FRBNY Study.")

One of the major benefits of a home mortgage bridge loan assistance program is that it helps to avoid both unnecessary foreclosures and restructuring-related complications. Such a program avoids unnecessary foreclosures precisely by dint of its capitalizing upon the fact that many foreclosures stem, not from unsound mortgage loan structures or the fundamental non-creditworthiness of borrowers, but simply from *temporary income loss*. For the same reason, a well-structured bridge loan assistance program can also become substantially self-perpetuating through borrower repayment of principal and interest on underlying loans once regular incomes are restored. It also bears noting that business cycles have historically been part of the economic fabric of the state and the nation. A bridge loan mortgage payment assistance program to address the current economic crisis can accordingly be expected to prove helpful in connection with future, more conventional economic downturns as well.

HEMAP, which has a track record of over 25 years, provides sufficient data on which to judge performance and recommend a similar, but improved, program for New York and elsewhere. The Bill makes use of the data gleaned from over 30 years' experience with HEMAP. Key measures of HEMAP's success are: (1) the extent to which the program prevents borrowers from losing their homes; and (2) the extent to which loans are repaid. Given that around 80% of HEMAP loan recipients have retained their residences and repaid their mortgage loans in full, both performance measures are favorable in its case.

Because a bridge loan mortgage assistance program is tailored to helping financially troubled homeowners who are most likely to avoid foreclosure if assisted financially, it is not a comprehensive solution to the mortgage crisis or to the broader economic crisis. It is, however, one potentially effective arrow in the state's quiver for addressing certain important aspects of the current economic crisis, with potentially wide-ranging effects if adopted in other states or by the federal government.

QUALIFICATIONS FOR BRIDGE LOAN MORTGAGE ASSISTANCE

Bridge loans under HMBLAA would be available for the payment of mortgages on 1-to 4-family residences and for single-family residences in condominiums, housing cooperatives or manufactured homes located in New York. The mortgaged property would also have to be the mortgagor's principal residence; the mortgagor could not own other residential property subject to a mortgage lien. The mortgagor must be suffering temporary financial hardship due to unemployment, underemployment, or other cause specified by regulation, under circumstances beyond his or her control. Furthermore, the mortgagor must not have been more than sixty days delinquent on any residential mortgage (a) within 5 years preceding the delinquency for which assistance is requested, or (b) within 5 years prior to filing for assistance, if the mortgagor is not contractually delinquent at the time of such filing. The only exception to a delinquency within the 5 year time period is when the mortgagor can demonstrate that the prior mortgage delinquency itself resulted from circumstances beyond his or her control.

A determination as to whether the financial hardship is temporary is tied to the likelihood that the mortgagor will prove able to resume full mortgage payments not later than 24 months after the commencement of bridge loan assistance payments. In periods of high unemployment, this period may be extended to 36 months. Factors considered in making a determination that financial hardship is temporary and that the mortgagor will be in a position to resume making full mortgage payments within 24 or 36 months include prior work history, opportunities for retraining, noncash benefits that increase the household's ability to defray expenses, potential for repaying short-term debt, a favorable work and credit history, and any other relevant factors necessary to determine whether financial hardship is temporary. An applicant who has quit or been fired from paid employment is not eligible for assistance.

Bridge loan assistance probably should *not* be extended to mortgagors in upper income brackets. Mortgagors with higher incomes typically have more resources to rely upon. Hence another important qualification for receiving bridge loan assistance under HMBLAA is that the borrower be classified as low, moderate, or middle income. For this purpose, the program defines eligible beneficiaries as mortgagors who, prior to the event triggering financial hardship, had income "that was less than 120% of the median family income for the metropolitan statistical area or statewide nonmetropolitan area where the property is located, as most recently determined and published by the Department of Housing and Urban Development."

TIMELINES FOR MAKING A BRIDGE LOAN AND ITS REPAYMENT

There are several possible bridge loan underwriting timelines under HMBLAA. One such timeline is triggered by mortgage delinquency. Another is triggered by a prospective beneficiary's filing for unemployment insurance. Where a mortgagor is at least 60 days contractually delinquent on his or her mortgage, the mortgagee or servicer must provide the mortgagor with a notice advising of the delinquency, the existence of HMBLAA and eligibility criteria, and the procedures for applying to the state for a mortgage assistance bridge loan. The mortgagor has 30 days to meet with a consumer credit counseling agency to resolve the delinquency by restructuring the loan through negotiations with the mortgagee. If, within 30 days of the mortgagor's contacting the agency, these negotiations are unsuccessful, the mortgagor has 10 days to apply for a mortgage assistance bridge loan.

Once an application is made, the state will notify all mortgagees that the application for a bridge loan is under consideration and that a determination will be made within 60 calendar days. No legal action may be taken by a mortgagee as long as all deadlines above are met. Nor, under HMBLAA, will compliance with this requirement in the form of abstention from legal action be permitted to prejudice the mortgagee's mortgage interest in the mortgaged property.

Mortgage bridge loan assistance programs typically are triggered by passage of some specified period of time after delinquency. The Bill works in this manner as well, while also providing for an additional, important alternative to this trigger. That is, in the case where a mortgagor files for unemployment insurance, the New York State Department of Labor will notify the filer that mortgagors may be eligible for bridge loan mortgage assistance if, due to a loss of income, they anticipate that there will not be sufficient income to make timely payments on their mortgages without drawing down assets or taking on additional debt. If the mortgagor applies to the state for mortgage bridge loan assistance, the state will notify the mortgagor of its decision within 60 calendar days of receipt.

This alternative is important because in some cases, this path to mortgage bridge loan assistance might not be taken or even available absent the automatic trigger. For there will likely be some mortgagors who simply draw down assets or rely upon other resources until the point where they either anticipate default or are 60 days delinquent on their mortgages. Other mortgagors, in their distress, doubtless will overlook or misunderstand the notices they receive that inform them that bridge loan assistance may be available.

MECHANICS OF A BRIDGE LOAN MORTGAGE ASSISTANCE PROGRAM

An application for a bridge loan will be the result of a loss of income due to temporary unemployment which makes the mortgagor incapable of making monthly principal and interest payments after deducting necessary living expenses from remaining income, including any government support payments. The HMBLAA administrator will determine the portion of income received by the mortgagor that is necessary to cover reasonable living expenses. Income above the amount needed for necessary living expenses, will be used to pay part of the monthly principal and interest on the mortgage loan and HMBLAA will cover the remaining portion. The portions of monthly principal and interest paid by HMBLAA are essentially recurring loans to the mortgagor. When the mortgagor regains employment which provides income sufficient to pay living expenses and monthly principal and interest payments, the loans will cease and the mortgagor will once again have sole responsibility for making principal and interest payments on the mortgage loan. At that point, interest will start to accrue on the aggregate amount of the loans and the mortgagor will start making principal and interest payments on the aggregate amount of loans.

The mortgagor will receive the loans for 24 or 36 months. These periods may not be extended. In addition, if at some point the mortgagor has sufficient equity in the house or income or both to refinance at market rates, the state will stop making loans. If the mortgagor’s income is not enough to pay principle and interest before the loans stop, than the state has made a bad underwriting decision; it misjudged the mortgagor’s ability to find employment within 24 or 36 months that provides income to cover living expenses, principle and interest on the mortgagee’s loan and principle and interest on the state’s recurring loans (Although, in the case of the state, if the mortgagor has income sufficient to cover living expenses and principle and interest on loan from the mortgagee, it would likely suspend its right to payment until the mortgagor’s income increased further.). The bank can foreclose (or the mortgagor can sell the house) and take the equity in the house to pay off the remainder of its loan. If there is enough equity left over, the state has a claim on that amount to pay off its loans.

FUNDING FOR THE MORTGAGE BRIDGE LOAN ASSISTANCE PROGRAM

If HEMAP is any guide, a program such as the one proposed by the Bill can be quite efficiently and cost-effectively run, and can accordingly save the state more in the way of costs occasioned by unnecessary foreclosures than it occasions in the way of expenditure. HEMAP was initially “start-up” funded entirely by the state of Pennsylvania through an appropriation of $25 million in 1984. However, although subsequent state appropriations averaged $10 million annually from 2005 to 2009, for over 80% of HEMAP’s history the program has relied mainly on proceeds from repayment of existing loans. The cost per application processed is $320, or about $4.5 million, to administer the program annually. The average monthly supplemental bridge loan to a borrower is approximately $500.

A determination whether to adopt HMBLAA should be based on weighing the comparatively modest costs of running the program against the much heftier costs of depressed housing prices, negative effects on housing stock, increased demands on police and firemen associated with abandoned properties, loss of tax base, increased demands on the court system and services to displaced families, and a host of other social ills associated with mass evictions and deteriorating neighborhoods. Costs must also be borne by lenders and investors due to lost or reduced mortgage payments, property maintenance, vandalism, legal fees and reduced resale values.

Given the nature of the current mortgage crisis, it is in the interest of homeowners, lenders, the legislature and others to find workable, cost-effective solutions to preventable foreclosure. Even those individuals who have not been directly affected by foreclosure will benefit from avoiding the associated negative externalities. The Bill provides that startup funds for the program shall be made available through state appropriations to the extent that such funding is available, with the program thereafter to be funded through the following means: (1) repayments of mortgage bridge loan assistance to the state; (2) continuing state appropriations; (3) contributions made available by firms in return for tax credits; (4) charitable contributions made available by any party; and (5) contributions by financial institutions to fulfill their state and federal Community Reinvestment Act obligations.[3]

CONCLUSION

For the foregoing reasons, the City Bar supports enactment of the Home Mortgage Bridge Loan Assistance Act.

January 2014

[3] Under both the federal and New York CRA, banks are periodically evaluated to determine how well they meet the credit needs of the communities ("assessment areas") they serve through lending activities, the provision of other financial services, and qualified investments. If funding is structured properly, banks may receive qualified CRA investment credit by helping to fund the HMBLAA bridge loan assistance program. The federal CRA provides that an investment is "qualified" for CRA credit if it has as its primary purpose "community development". An investment will be deemed to have community development as its primary purpose if it is designed for the express purpose of revitalizing or stabilizing low- or moderate-income areas, or providing affordable housing for or community services to low- to moderate-income persons. Both the federal financial regulators and the New York State Department of Financial Services have permitted banks wide latitude in meeting their obligations and responsibilities under their CRAs. While HMBLAA does not seek to modify mortgages, it does seek to prevent foreclosures and will serve as a means of stabilizing communities. Grants to the HMBLAA program would therefore appear to be qualifying investments under both CRAs. The regulations also recognize that community development programs, such as HMBLAA will be, can operate on a statewide basis. Thus a bank's contribution to HMBLAA would be considered a qualified investment even if there are no HMBLAA participants in that bank's assessment area. For additional detail concerning the eligibility of banks for contributions to HMBLAA as "qualified investments" under the federal and New York CRA, see *Supplemental Report to Adopt the Home Mortgage Bridge Loan Assistance Act*, New York City Bar Association Banking Law Committee (December 2013) available at http://www2.nycbar.org/pdf/report/uploads/HomeMortgageBridgeLoanCRAFundingSuppReportFINAL12.23.13.pdf.